85-148

No. ____

Office-Supreme Court, U.S.
FILED
JUL 26 1985
ALEXANDER L. STEVAS,
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

BLUE CROSS and BLUE SHIELD OF MICHIGAN,
a nonprofit Michigan corporation,

Appellant,

—against—

WILLIAM G. MILLIKEN, Governor of the State of Michigan, FRANK J. KELLEY, Attorney General of the State of Michigan, and NANCY A. BAERWALDT, Commissioner of Insurance of the State of Michigan,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF MICHIGAN

JURISDICTIONAL STATEMENT

Of Counsel:
RANDOLPH S. SHERMAN
JOEL KATCOFF

Of Counsel:
WILLIAM M. SAXTON
KEEFE A. BROOKS
Butzel Long Gust Klein
& Van Zile
1881 First National Building
Detroit, Michigan 48226
(313) 963-8142

STANLEY D. ROBINSON
Kaye, Scholer, Fierman,
Hays & Handler
425 Park Avenue
New York, New York 10022
(212) 407-8000

Attorney for Appellant

QUESTION PRESENTED

Did the State of Michigan violate the Fifth and Fourteenth Amendments of the Constitution of the United States by taking control of a private, nonprofit health care corporation from its corporate membership without paying just compensation?

TABLE OF CONTENTS

PAGE

QUESTION PRESENTED i

TABLE OF AUTHORITIES iv

OPINIONS BELOW 1

JURISDICTION 2

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED 2

STATEMENT OF THE CASE 5

1. Blue Cross and Blue Shield of Michigan 5
2. PA 350 9
3. The Proceedings Below 12

THE QUESTION PRESENTED IS SUBSTANTIAL ... 15

1. By Taking The Corporate Membership's Control Over BCBSM, Michigan Has Divested Private "Property" 17
2. PA 350's Divestiture Of The Corporate Membership's Control Over BCBSM Is An Unconstitutional "Taking" 19
3. Since Michigan Has Not Provided For Just Compensation, BCBSM Is Entitled To An Injunction . 24

CONCLUSION 25

PAGE

APPENDIX (separately bound):

Opinion of the Michigan Supreme Court, April 16, 1985 (reported at 422 Mich. 1; 367 N.W.2d 1) 1a

Ingham County Circuit Court Order of Preliminary Injunction, April 2, 1981..... 130a

Ingham County Circuit Court Order of Preliminary Injunction, July 31, 1981..... 132a

Michigan Supreme Court Order Directing Circuit Court to Certify Controlling Questions of Public Law, March 25, 1982..... 134a

Ingham County Circuit Court Certification of Controlling Questions of Public Law and Statement of Need to Conduct Evidentiary Hearings, April 15, 1982.... 138a

Ingham County Circuit Court Findings of Relevant Facts, November 1, 1982..... 149a

Ingham County Circuit Court Supplement to Findings of Relevant Facts, November 9, 1982 ..... 243a

Michigan Supreme Court Judgment, April 16, 1985.... 245a

Michigan Supreme Court Order Denying Motion for Rehearing, June 24, 1985..... 247a

Notice of Appeal, July 10, 1985..... 249a

Michigan Nonprofit Health Care Corporation Reform Act, 1980 PA 350, MCL 550.1101 *et seq.*; MSA 24.660 (101) *et seq*..... 251a

TABLE OF AUTHORITIES

Cases: PAGE

Andrus v. *Allard*, 444 U.S. 51 (1979) ..... 22n.

Baltimore County Hospital v. *Maryland Hospital Service, Inc.*, 234 Md. 427, 200 A.2d 39 (1964) ..... 18n.

Berman v. *Parker*, 348 U.S. 26 (1954)..... 20

Blue Cross and Blue Shield of Michigan v. *Demlow*, 403 Mich. 399, 270 N.W.2d 845 (1978).....6n., 9, 24

Blue Cross of Iowa v. *Foudree*, Civ. Action No. 84-597-A (S.D. Iowa, May 2, 1985)..... 16

Board of Regents v. *Trustees of Endowment Fund*, 206 Md. 559, 112 A.2d 678, *cert. denied*, 350 U.S. 836 (1955) 19

Fein v. *Lansten Monotype Machine*, 196 Va. 753, 85 S.E.2d 353 (1955) ..... 17n.

Hawaii Housing Authority v. *Midkiff*, 104 S. Ct. 2321 (1984) 20

Kaiser Aetna v. *United States*, 444 U.S. 164 (1979) 21

Klaus v. *Hi-Shear Corp.*, 528 F.2d 225 (9th Cir. 1975) . 17n.

Loretto v. *Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982).....16, 21, 22

Minnesota Baptist Convention v. *Pillsbury Academy*, 246 Minn. 46, 74 N.W.2d 286 (1955)..... 18

Ohio v. *Neff*, 52 Ohio St. 375, 40 N.E. 720 (1895)..... 19

Opinion of the Justices, 373 So. 2d 293 (Ala. 1979).... 19

Opinion of the Justices, 333 So. 2d 125 (Ala. 1976).... 17n.

Penn Central Transportation Co. v. *New York City*, 438 U.S. 104 (1978). .....16, 21, 22n.

PAGE

Rassner v. *Federal Collateral Society*, 299 Mich. 206, 300 N.W. 45 (1941) 17

Ruckelshaus v. *Monsanto Co.*, 104 S. Ct. 2862 (1984) 17, 19, 20, 21, 23

State v. *North Star Research and Development Institute*, 294 Minn. 56, 200 N.W.2d 410 (1972) 18

State ex rel. Waring v. *Georgia Medical Society*, 38 Ga. 608 (1869) 19

United States v. *General Motors Corp.*, 323 U.S. 373 (1945) 17

Weiner v. *Hospital Service Plan of Lehigh Valley*, 187 Pa. Super. 244, 144 A.2d 575 (1958) ..... 18n.

Westland Convalescent Center v. *Blue Cross & Blue Shield of Michigan*, 414 Mich. 247, 324 N.W.2d 851 (1982) ..... 18n.

Constitutional Provisions:

U.S. Const. amend. V ..... *passim*

U.S. Const. amend. XIV, § 1 ..... *passim*

Statutes:

28 U.S.C. § 1257(2) 2

Michigan Nonprofit Health Care Corporation Reform Act, 1980 PA 350, MCL 550.1101 *et seq.*; MSA 24.660 (101) *et seq.* ..... *passim*
§ 203 ..... 3, 11, 24
§ 205(4) 20
§ 207(1) 12
§ 301(1) 3, 10
§ 301(2) 3, 10
§ 301(3) 3, 10

PAGE

§ 301(4) 3, 10
§ 301(5) 3, 10
§ 301(6) 3, 11
§ 301(7) 4, 11, 24
§ 302(1) 4, 11, 24
§ 305(1) 4, 11, 24
§ 305(2) 12
§ 502(1) 20
§ 504(1) 10, 20
§ 505(2) 10
§§ 506-13 10
§ 516 10
§ 607(1) 20
§ 701(1) 5

Michigan Act 108 of 1939 ..... 6, 10

Michigan Act 109 of 1939 ..... 6, 10

Other authorities:

2 W. Blackstone, Commentaries, *405 23

14 Fletcher, *Cyclopedia of the Law of Private Corporations* § 6708 (1980 Rev.) ..... 17n.

J. Locke, The Second Treatise of Civil Government, Ch. 5 (J. Gough ed. 1947) 23

18 Am. Jur. 2d *Corporations* § 477 (1965) 19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

No. ____

BLUE CROSS and BLUE SHIELD OF MICHIGAN, a nonprofit Michigan corporation,[1]

Appellant,

—against—

WILLIAM G. MILLIKEN, Governor of the State of Michigan, FRANK J. KELLEY, Attorney General of the State of Michigan, and NANCY A. BAERWALDT, Commissioner of Insurance of the State of Michigan,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF MICHIGAN

JURISDICTIONAL STATEMENT

OPINIONS BELOW

The opinion of the Supreme Court of Michigan is reported at 422 Mich. 1, 367 N.W.2d 1 (1985) and is included in the appendix at pp. 1a-129a. The dissenting opinion of Justice Levin begins at 422 Mich. at 97; 367 N.W.2d at 48 (Appendix at 89a).[2]

1 Blue Cross and Blue Shield of Michigan is a non-stock corporation which has no subsidiary or affiliated corporations except those that are wholly owned.

2 Page references herein to the opinions below will be to the appropriate page in Michigan Reports. The Michigan Reports pagination is reproduced in the appendix.

JURISDICTION

This is an appeal by Blue Cross and Blue Shield of Michigan ("BCBSM"), a nonprofit health care corporation, from a decision of the Michigan Supreme Court dated April 16, 1985 upholding certain provisions of Michigan's Nonprofit Health Care Corporation Reform Act, 1980 PA 350 ("PA 350"), MCL 550.1101 *et seq.*; MSA 24.660(10l) *et seq.*, against a challenge under the Taking Clause of the Fifth Amendment, made applicable to the States by the Due Process Clause of the Fourteenth Amendment.[3] The Supreme Court of Michigan denied a timely petition for rehearing on June 24, 1985. A notice of appeal to this Court was duly filed in the Supreme Court of Michigan on July 10, 1985. This Court has jurisdiction pursuant to 28 U.S.C. § 1257(2).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The Fifth Amendment to the Constitution of the United States provides in pertinent part:

> "nor shall private property be taken for public use, without just compensation."

The Fourteenth Amendment to the Constitution of the United States provides in pertinent part:

> "nor shall any State deprive any person of life, liberty, or property, without due process of law."

The Michigan Nonprofit Health Care Corporation Reform Act, 1980 PA 350, MCL 550.1101 *et seq.*; MSA 24.660 (10l) *et seq.* provides in pertinent part:

---

3 The Michigan Supreme Court also resolved a number of other constitutional challenges to PA 350. Only the majority's rejection of the Taking Clause challenge is raised on this appeal.

"By action of its board of directors, a health care corporation may integrate into a single instrument the provisions of its articles of incorporation . . . . If the restated articles restate and integrate and also further amend the articles, they shall also be adopted by the board of directors." § 203.

"The property and lawful business of a health care corporation shall be held and managed by a board of directors to consist of not more than 35 members." § 301(1).

"Four voting members of the board shall be representatives of the public appointed by the governor by and with the advice and consent of the senate." § 301(2).

"The board of directors shall consist of not more than 25% provider directors." § 301(3).

"The bylaws of a health care corporation may authorize not more than 1 officer or employee of the corporation to serve as a voting or nonvoting director." § 301(4).

"The remaining members of the board of directors shall include representatives of large subscriber groups, medium subscriber groups, small subscriber groups, and nongroup subscribers, in proportions which fairly represent the total subscriber population of the health care corporation. However, at least 3 directors shall represent nongroup subscribers, . . . and at least 3 directors shall represent small subscriber groups. Large and medium subscriber groups shall be represented, to the greatest extent possible, by an equal number of labor and management representatives and shall be categorized as labor subscriber representatives or management subscriber representatives." § 301(5).

"The method of selection of the directors, other than the directors who are representatives of the public . . . shall be specified in the bylaws." § 301(6).

"The method of selection of each category of subscribers entitled to representation on the board under subsection (5) shall maximize subscriber participation to the extent reasonably practicable. This subsection shall permit, but not require, the statewide election of a director or member of the corporate body. The method of selection shall neither permit nor require nomination, endorsement, approval, or confirmation of a candidate or director by the corporate body, the board of directors, or the management of the health care corporation, or any member or members of any of these. This subsection shall not apply to the selection of an officer or employee as a director pursuant to subsection (4). This subsection shall not limit the rights of any director, member of the corporate body, or employee or officer of the health care corporation to participate in the selection process in his or her capacity as a subscriber, to the same extent as any other subscriber may participate." § 301(7).

"The board of directors shall adopt initial bylaws and may amend or repeal those bylaws or adopt new bylaws, subject to the prior approval or certification by the attorney general. The bylaws may contain any provision for the regulation and management of the affairs of the health care corporation not inconsistent with the articles of incorporation, this act, or any other applicable provision of law." § 302(1).

"A health care corporation may establish a corporate body. The corporate body shall consist of individuals selected in the same manner as individuals are selected to serve as nonpublic members on the board of directors. The size of the corporate body shall be such that, for each nonpublic voting director on the board of directors of the corporation, there are 2 members of the corporate body." § 305(1).

"Each health care corporation on the effective date of this act shall be subject to this act without formal reor-

ganization under this act, and shall be considered to exist under this act. However, within 120 days following the effective date of this act, the health care corporation shall do all of the following:

(a) Amend its articles of incorporation and bylaws to conform to the requirements of this act, subject to the certification of the attorney general . . . .

(b) Restructure its board of directors to conform with the requirements of this act. . . .

(c) After complying with subdivisions (a) and (b), obtain from the commissioner a new certificate of authority." § 701(1).

PA 350 is included in its entirety in the appendix at 251a-353a.

STATEMENT OF THE CASE

1. Blue Cross and Blue Shield of Michigan

BCBSM is a private, nonprofit membership corporation providing prepaid health care coverage to approximately half of Michigan's population. It has no shareholders. Instead, BCBSM is comprised of 93 corporate members. The corporate membership's control over BCBSM derives from its articles of incorporation and bylaws, pursuant to which the membership has sole authority to elect BCBSM's board of directors. BCBSM's membership is also self-perpetuating: it has sole authority to select its own members.

BCBSM had its genesis as a result of the Great Depression in the 1930's when "pervasive poverty among the people caused them to forgo needed health care services which, in turn, resulted in financial uncertainty for hospitals and physicians." 422 Mich. at 13. To alleviate this problem, hospitals and physicians formed BCBSM's two corporate predecessors, the Michigan Society for Group Hospitalization ("MSGH") and the Michigan Medical Service ("MMS").

MSGH was incorporated on October 3, 1938 under the general nonprofit corporation law by several community hospitals in Michigan. The incorporators contributed $10,000 to MSGH's initial working capital and they, together with others chosen by them, formed the original corporate membership. In December 1939, MSGH amended its articles of incorporation to come under Michigan's health care corporation enabling legislation, Act 109 of 1939 ("PA 109").

In July 1939, pursuant to Michigan's companion health care statute, Act 108 of 1939 ("PA 108"), doctors under the auspices of the Michigan State Medical Society incorporated MMS with a cash contribution of $16,000. The original corporate membership consisted of the incorporators.

PA 108 and 109 declared health care corporations to be charitable and benevolent institutions, exempt from taxation. The statutes provided for the regulation of health care corporations by the Commissioner of Insurance in certain limited respects,[4] but the legislature did not interfere with corporate governance and control. Indeed, PA 108 and 109 touched upon corporate governance only in the following respects: (1) the initial bylaws of MSGH and MMS were to be reviewed by the Commissioner of Insurance for compliance with the statutes; (2) MSGH's board of directors was required to have not less than nine persons, with representation of participating hospitals, physicians and the public; (3) the board of directors of MMS was required to have "representation from the public and the medical profession"; (4) directors of both corporations were to be elected for a term of one year unless the articles or bylaws prescribed a longer term or staggered terms; and (5) a majority of directors was to constitute a quorum for the transaction of business. Corporate governance and control were otherwise left to the corporate memberships. In particu-

---

4 The Commissioner was authorized to review and approve health care contracts to assure that they did not "work a fraud" on subscribers, that the rates charged and the benefits provided were fair and reasonable and that adequate reserves were maintained. Blue Cross and Blue Shield of Michigan v. Demlow, 403 Mich. 399, 270 N.W.2d 845 (1978).

lar, the corporate memberships of MSGH and MMS were free to control the selection of their respective boards of directors and the selection of their respective members.

Over the next several decades, MSGH (which became known as Blue Cross) and MMS (which became Blue Shield) voluntarily increased consumer (or "subscriber") representation on their respective boards of directors to a point where subscribers eventually constituted a majority.[5] The authority to elect all of the directors, however, remained vested in the corporate memberships.

Similarly, Blue Cross and Blue Shield voluntarily invited representatives of corporate groups, labor unions and other subscribers of health care plans to join their respective corporate memberships. The method of selecting members remained unchanged: nominees were elected by the membership as a whole.

Effective January 1, 1975, Blue Cross and Blue Shield were consolidated to create a new corporation, BCBSM. Under the Plan of Consolidation, BCBSM's corporate membership was comprised initially of the boards of directors of Blue Cross and Blue Shield, which had previously been chosen by the respective corporate memberships.

Today, BCBSM's corporate membership is comprised of 93 persons, as follows:

a. Consumers-groups:	28 representatives of substantial group purchasers of BCBSM coverage, such as Ford, General Motors and Chrysler.
b. Consumers-labor:	10 representatives of unions which have substantial memberships enrolled in BCBSM health care plans.

5 In 1971, MMS also decided to allow two of its directors to be nominated by the Commissioner of Insurance.

c. Consumers-at-large:	12 consumers who shall be subscribers to BCBSM, influential in the community and not representative of another component.
d. Consumers-appointed:	4 consumers named by the Insurance Commissioner who do not hold elective office, are not government employees and are not affiliated with the insurance industry.
e. Doctors of medicine:	14
f. Doctors of osteopathy:	4
g. Hospital representatives:	18
h. Pharmacists:	2
i. President of BCBSM	

The 47 members of BCBSM's board of directors are drawn from the corporate membership. Each of the constituent groups comprising BCBSM's corporate membership is proportionately represented on its board.[6]

---

6 Consumer-group representatives on the board of directors come from groups of over 500 subscribers in the Detroit area and over 250 subscribers outside of that area. Past practice has been to include representatives of the five largest groups on the board of directors. These groups are Ford Motor Company, General Motors Corporation, Chrysler Corporation, Michigan Bell and the Michigan Farm Bureau. The current consumer representatives include such persons as: Charles Chomet, project manager for Citizens for Better Care, Inc.; Beverley C. McDonald, deputy director of Michigan Legal Services, Inc.; Robert E. Braden, administrative director of the Michigan Farm Bureau; Ellsworth G. Reynolds, president of Detroit College of Law; and five representatives of the UAW and AFL-CIO. The current chairman of the board is James W. Woodruff, who was originally nominated to the board by the Insurance Commissioner.

The members of BCBSM all have a vital economic stake in BCBSM. The corporate subscriber members and labor unions engage in collective bargaining negotiations over the level and type of health care benefits and are therefore acutely interested in BCBSM's ability to offer, at a reasonable price, what they deem to be appropriate prepaid coverage. The individual subscribers of BCBSM likewise have an obvious economic interest in the cost of prepaid medical care and the benefits offered. Finally, the providers of health care have the same economic interest which caused them to form BCBSM's predecessors in the first place: alleviating the financial uncertainty resulting from the inability of the public to pay for health services.

Thus, the members of BCBSM have a community of interest in the successful operation of BCBSM. This collective economic interest served as a powerful incentive for the membership—through its chosen board of directors—to build BCBSM into the valuable enterprise that it is today. As recognized by the Michigan Supreme Court, the preeminent position that BCBSM occupies in the health care market today is attributable at least in part to "the expertise and aggressiveness of its management." 422 Mich. at 15. That management, since BCBSM's inception, has always been under the sole control of its corporate membership.

2. PA 350

In *Blue Cross and Blue Shield of Michigan* v. *Demlow*, 403 Mich. 399, 270 N.W.2d 845 (1978), the Michigan Supreme Court held that under BCBSM's enabling legislation, PA 108 and 109, the Commissioner of Insurance had *no* power to regulate the rates of payment to physicians, and *no* power to order BCBSM to implement hospital cost containment programs. 270 N.W.2d at 847. The court explained that "[m]anagement of the corporation has been specifically entrusted to the board of directors, not to the Commissioner." *Id.* at 855.

In the wake of *Demlow*, and in response to a perception that BCBSM had not succeeded in containing the rapid escalation of health care costs, PA 350, which repealed PA 108 and 109, was enacted on December 29, 1980. As explained below, the new law utilizes two fundamentally different approaches to the problem of rising costs.

First, the act seeks to address the problem by *regulation*. It broadens the Commissioner's power so as to include for the first time regulation of BCBSM's rates of payment to physicians, and it sets forth specific criteria to be followed by the Commissioner in exercising that power with respect to both physician and hospital services. PA 350 §§ 505(2), 506-13, 516. Moreover, the act requires BCBSM to enter into provider class plans which must conform to specific statutory cost containment goals. PA 350 § 504(1). And, finally, it gives the Commissioner power to correct deficiencies in those plans if the prescribed goals are not met. PA 350 §§ 510-13.

Second, the act seeks to curb escalating health care costs by *transferring corporate control*. Through a series of related provisions, control of BCBSM is taken from the corporate membership and delivered to persons who, the legislature believes, will be more responsive to consumer needs. The act strips the corporate membership of *all* of its rights: the right to elect the board of directors, the right to amend the articles of incorporation and bylaws, and the right to determine its own membership.

Section 301 of the statute limits BCBSM's board of directors to 35 persons, and stipulates that four of them must be "representatives of the public" appointed by the governor. PA 350 §§ 301(1), 301(2). Not more than 25% (*i.e.*, eight members) of the board may consist of health care provider representatives, and not more than one director may be a BCBSM officer or employee. PA 350 §§ 301(3), 301(4). The remaining 22 members of the board of directors must include representatives of large, medium and small subscriber groups and non-group subscribers. PA 350 § 301(5).

But the legislature did far more than merely change the composition of the board of directors. The corporate membership is expressly divested of its right to exercise any control or even influence over the selection of BCBSM's board:

> "The method of selection shall neither permit nor require nomination, endorsement, approval, or confirmation of a candidate or director by the corporate body, . . . or any member or members . . . ." PA 350 § 301(7).

Rather, the act requires a method of selection of the directors, which is to be specified in the bylaws, that must "maximize subscriber participation to the extent reasonably practicable." PA 350 §§ 301(6), 301(7). Toward that end, a statewide election is authorized, although not mandated. PA 350 § 301(7).[7]

BCBSM's membership is deprived not only of its right to elect the board of directors, but also of its right to determine its own members. Section 305(1) of the act permits a health care corporation to establish a corporate body, but it must be no larger than twice the size of the 35-person board of directors. This provision automatically reduces the membership to 70, thereby ousting 23 members. What is more, the act decrees that "[t]he corporate body shall consist of individuals selected in the same manner as individuals are selected to serve as nonpublic members of the board of directors." PA 350 § 305(1). BCBSM's membership is thus denied the right to select its own members and thereby determine its own succession.

The act also strips the corporate membership of its power to amend BCBSM's articles of incorporation and bylaws and gives that power to the newly-elected board of directors. PA 350 §§ 203, 302(1). Corporate members are allowed only a

---

7 Only to the extent that corporate members are also subscribers are they even permitted to participate in the election of the board:

> "This subsection shall not limit the rights of any . . . member of the corporate body . . . to participate in the selection process in his or her capacity as a subscriber, to the same extent as any other subscriber may participate." PA 350 § 301(7).

token role in BCBSM's governance: they "may serve on committees of the board of directors." PA 350 § 305(2). Whether they will be accorded even this limited opportunity to participate in the affairs of BCBSM is thus subject to the absolute control of the new board of directors.

The corporate membership's loss of its right to select the board of directors is highly significant in light of the board's extensive managerial powers. Although subject to the regulatory authority of the Insurance Commissioner, management of the corporation remains vested in its board of directors, which retains broad authority to establish its lines of business, devise health care plans, establish rates, enter into contracts, invest funds, borrow money, guarantee loans, dispose of property and even dissolve the corporation. 422 Mich. at 48; PA 350 § 207(1). Under PA 350, this broad managerial authority is to be exercised by a board of directors neither selected by the corporate membership nor accountable to it.

3. The Proceedings Below

PA 350 was scheduled to go into effect on April 3, 1981. On March 20, 1981, BCBSM filed a complaint against Michigan's Governor, Attorney General and Commissioner of Insurance in the Ingham County Circuit Court seeking a declaratory judgment that PA 350 violated the United States and Michigan Constitutions in a multiplicity of respects. At the same time, it sought preliminary injunctive relief against enforcement and operation of the statute. On April 2, 1981, the Circuit Court granted BCBSM's motion for a preliminary injunction.

Almost a year later, on March 15, 1982, Governor Milliken, pursuant to Michigan law, asked the Michigan Supreme Court to determine controlling questions of public law concerning the constitutionality of PA 350. The Michigan Supreme Court, in turn, entered an order requesting the Circuit Court to certify the pertinent controlling questions involved in this action and provide a statement of relevant facts. On November 1, 1982, after evidentiary hearings, the Circuit Court filed its certified questions of law and findings of fact.

More than two years later, on April 16, 1985, the Michigan Supreme Court issued its decision in this case—a case which it described as presenting "important [constitutional] questions of first impression." 422 Mich. at 9. Although the Court invalidated certain provisions of PA 350 and declined to address others because of the lack of an actual controversy, it upheld the key sections of the act against BCBSM's constitutional challenges. In particular, the Court held, over Justice Levin's vigorous dissent, that in divesting the corporate membership of control of BCBSM, PA 350 did not unconstitutionally "take" private property without payment of just compensation.

The Michigan Supreme Court acknowledged that BCBSM's board of directors has historically "been nominated from the corporate members and elected by the same body with the exception of two public appointees of the Insurance Commissioner." 422 Mich. at 15. Moreover, the Court conceded that PA 350 effectively "divest[s] the members of the *sole authority* they previously possessed to determine the method of selection of BCBSM's corporate management" (422 Mich. at 32); "dispossesse[s] the members of the *sole authority* they previously held to determine the method of selection of BCBSM's corporate membership" (422 Mich. at 65); and "divest[s]" the corporate membership "of the direct power they formerly held to alter the articles and bylaws"—which the Court described as a "considerable impairment" since "the power to elect the corporate body and board is derived from" those corporate documents (422 Mich. at 61-62). Nevertheless, the Court swept aside BCBSM's contention that such a divestiture and dispossession of the right to control the corporation was an unconstitutional taking of private property without just compensation. 422 Mich. at 46-47.

The Court's treatment of the "taking" issue rested on two premises. First, notwithstanding the repeated holdings of this Court that a taking pursuant to a valid exercise of the police power must nevertheless be compensated, the state court thought that "losses incident to the lawful exercise of the police

power are noncompensable." 422 Mich. at 46. Second, the Michigan court opined that the members of BCBSM, a regulated, nonprofit corporation, had no "investment-backed expectations" which could give rise to a compensable property interest. 422 Mich. at 47.

In his dissenting opinion, Justice Levin reasoned that the power to use, control and dispose of property is the core attribute of property ownership (422 Mich. at 99, 102); that "[w]hen the state redistributes control, it has gone beyond mere regulation and has taken *both* control and the assets, properties and business subject to control" (422 Mich. at 102); that the property interest represented by corporate control may not constitutionally be appropriated by the state without just compensation merely because BCBSM is a nonprofit corporation (422 Mich. at 113-19); that the incorporators—the direct predecessors of BCBSM's present members—established BCBSM with contributions of cash, labor and initiative, so that the corporate membership had an investment-backed expectation in the right to govern BCBSM, subject to the regulatory authority of the Commissioner of Insurance (422 Mich. at 115-19); and that nothing in the regulatory history of BCBSM—PA 350 having been enacted in the wake of *Demlow* precisely because the Commissioner lacked sufficient statutory authority to regulate BCBSM (422 Mich. at 119-21)—gave "the organizers of the BCBSM constituent corporations and of BCBSM and the members thereof" any reason to anticipate "that the Legislature might seek to so transform the governance of BCBSM" (422 Mich. at 122).

BCBSM moved the Michigan Supreme Court for rehearing on May 7, 1985. That motion was denied on June 24, 1985. On the same date, BCBSM applied to this Court (Hon. Sandra Day O'Connor) for an order partially staying the judgment of the Michigan Supreme Court pending final disposition of this appeal. That application was denied on July 1, 1985.[8]

---

8 In opposing BCBSM's stay application, appellees made the astounding assertion that the taking issue presented on this appeal was neither

THE QUESTION PRESENTED IS SUBSTANTIAL

The holding below that a state may constitutionally strip the corporate membership of a nonprofit health care corporation of its right to control the corporation was based on grave misapprehensions of law. The ruling undermines the fundamental constitutional safeguard against the uncompensated governmental taking of private property for public use.

As Justice Levin noted, "[a]ll agree that a purpose of PA 350 is to eliminate control of BCBSM, and hence of its business and properties, by the persons presently in control and to transfer control to others, persons appointed by the Governor and elected by the providers and subscribers." 422 Mich. at 99. By transferring control of one of the state's major corporations, Michigan has vastly overstepped the bounds of regulation. It has utterly extinguished the proprietary rights of BCBSM's corporate membership, albeit for a perceived public purpose, without paying just compensation as required by the Fifth and Fourteenth Amendments.

Significantly, the Michigan Supreme Court did not question the property rights of the corporate membership. Indeed, as we

---

raised below nor resolved by the Michigan Supreme Court. They sought to create the impression that BCBSM's challenge to the corporate control provisions of PA 350 was based solely on the contract clause. But that contention is squarely refuted by the majority and dissenting opinions themselves. It could not be clearer that the Michigan Supreme Court flatly rejected BCBSM's "alleg[ation] that 1980 PA 350 has effectively removed from BCBSM control over its corporate direction" and thus effected "a taking of BCBSM's property without due process of law." 422 Mich. at 46. It is noteworthy that Justice Levin's lengthy dissent was devoted principally to the taking issue and never even reached the contract clause question.

The fact that BCBSM also attacked PA 350's corporate control provisions on other constitutional grounds—not raised on this appeal—is hardly an indication that those same provisions were not challenged under the taking clause. Indeed, the Michigan Supreme Court expressly noted that BCBSM had attacked essentially the same provisions on impairment-of-contract, due process and taking grounds. 422 Mich. at 43 n.34.

shall demonstrate, such property rights are well recognized under state law. Rather, the court below held that the extinguishment of those rights did not constitute a compensable "taking." In so holding, the court committed plain error at the very threshold of its analysis. "[I]t is clear," the court stated, "that losses incident to the lawful exercise of the police power are noncompensable." 422 Mich. at 46. However, as demonstrated below, *all* compensable governmental takings presuppose a "public use," *i.e.*, a lawful exercise of the police power. It is a "separate question . . . whether an otherwise valid regulation so frustrates property rights that compensation must be paid." *Loretto* v. *Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 425 (1982).

The court below committed further error in purporting to apply the standards of *Penn Central Transportation Co.* v. *New York City*, 438 U.S. 104 (1978), when it ruled that BCBSM's membership had no "investment-backed expectations" because the membership had no "discernible monetary or other equitable interest" in BCBSM. 422 Mich. at 47. As we will show, the court's holding not only disregarded the corporate membership's substantial economic interest in the corporation, but also misapplied *Penn Central*.

The significance of the erroneous ruling below transcends the interests of the parties to this litigation; it is of profound importance for the continued stability and vitality of the nation's health care and other nonprofit corporations. A federal district court has already relied on the decision below in rejecting a "taking" challenge to similar legislation disenfranchising the membership of a health care corporation. *Blue Cross of Iowa* v. *Foudree*, Civ. Action No. 84-597-A (S.D. Iowa, May 2, 1985). Indeed, if the decision below is permitted to stand, no nonprofit corporation will be secure against uncompensated governmental appropriation. Because, as the Michigan Supreme Court acknowledged, this case involves "important [constitutional] questions of first impression" (422 Mich. at 9), and because that court misapprehended and misapplied this Court's precedents, the issue presented on this

appeal is plainly substantial and calls for this Court's plenary consideration.

1. By Taking The Corporate Membership's Control Over BCBSM, Michigan Has Divested Private "Property"

The court below did not dispute the fact that the right of BCBSM's corporate membership to control the affairs of the corporation constitutes private "property." For it is well-established that the term "property" in the Taking Clause encompasses not only legal title, but also the right to control the *use* of property. *United States* v. *General Motors Corp.*, 323 U.S. 373, 377-78 (1945); *Ruckelshaus* v. *Monsanto Co.*, 104 S. Ct. 2862, 2873-74 (1984). As the Michigan Supreme Court itself pointed out on another occasion:

> "The term 'property', as used in the various guarantees against the taking of property without due process of law, is used in its most basic general sense . . . It includes not only title and possession, but also the right of acquisition and control, the right to make any legitimate use or disposal of the thing owned . . . ." *Rassner* v. *Federal Collateral Society*, 299 Mich. 206, 213-14, 300 N.W. 45 (1941).

For that reason, it is equally well-settled that the stockholders or members of a corporation—those who *control* the corporation's assets, properties and business through a board of directors of their selection—have a property interest in that control.[9] Neither government regulation of BCBSM nor its

---

9 Opinion of the Justices, 333 So.2d 125, 126-27 (Ala. 1976) (holding that giving a vote in the management of a corporation to lessees of the corporation's property "would deprive the members of their property rights in the management of the corporation without due process of law"); Fein v. Lansten Monotype Machine, 196 Va. 753, 85 S.E.2d 353, 361 (1955) ("[t]o deprive a stockholder of his right to vote is to deprive him of an essential attribute of his property"); Klaus v. Hi-Shear Corp., 528 F.2d 225, 234 (9th Cir. 1975) (under California law, "the right to vote a share of stock is a property right"); *see also*, 14 Fletcher, *Cyclopedia of the Law of Private Corporations* § 6708 (1980 Rev.) ("[t]he due process clause is violated by a regulation taking away the management and control of the corporation").

status as a nonprofit corporation negates the existence of that interest.

Private corporations subject to government regulation are nonetheless private. No one would contend that stockholders of commercial insurance companies or utilities have no private property interest in controlling the direction of those companies merely because they are regulated by the state. It is clear, therefore, that government regulation does not mean that BCBSM's membership lacks a property interest in controlling the corporation.

Similarly, although BCBSM is a nonprofit corporation serving certain public goals, it remains a *private* corporation.[10] Its members are its owners. *State* v. *North Star Research and Development Institute*, 294 Minn. 56, 200 N.W.2d 410, 414 (1972). Although they do not have an expectation of direct monetary gain from the operations of the corporation, their ownership interest is nonetheless valuable and important. Thus, referring to membership in a *nonprofit* corporation, the Minnesota Supreme Court has noted:

> "It is doubtful if any membership . . . right is any more important than the right to vote for the election of the directors . . . of a corporation who carry on and conduct the business of the corporation, elect or appoint its officers and agents, and in large measure, determine the manner in which the corporation operates." *Minne-*

10 It has been held that Blue Cross health care companies are private entities. Baltimore County Hospital v. Maryland Hospital Service, Inc., 234 Md. 427, 200 A.2d 39, 41 (1964); Weiner v. Hospital Service Plan of Lehigh Valley, 187 Pa. Super. 244, 144 A.2d 575, 578 (1958). Westland Convalescent Center v. Blue Cross & Blue Shield of Michigan, 414 Mich. 247, 324 N.W.2d 851 (1982), is not to the contrary: the dictum characterization in that case of BCBSM as a "quasi-public" entity was joined in by only two of seven members of the Michigan Supreme Court. Nor did the court below determine in this case whether BCBSM was a private or quasi-public corporation. In its view, there was no unconstitutional "taking"—not because BCBSM's corporate membership lacked a private property interest, but because the court believed deprivation of that interest did not constitute a compensable "taking."

sota Baptist Convention v. *Pillsbury Academy*, 246 Minn. 46, 61, 74 N.W.2d 286, 296 (1955).

Accord, Opinion of the Justices, 373 So. 2d 293 (Ala. 1979); *Board of Regents* v. *Trustees of Endowment Fund*, 206 Md. 559, 112 A.2d 678, *cert. denied*, 350 U.S. 836 (1955); *Ohio* v. *Neff*, 52 Ohio St. 375, 40 N.E. 720 (1895); *State ex rel. Waring* v. *Georgia Medical Society*, 38 Ga. 608, 626 (1869); 18 Am. Jur. 2d *Corporations* § 477 (1965).

In sum, the right of BCBSM's corporate membership to select the board of directors and its own membership succession, with the resulting control of the corporation's destiny, is a recognized property right. As we shall now demonstrate, the Court below erred in holding that Michigan could extinguish that right without the payment of just compensation.

2. PA 350's Divestiture Of The Corporate Membership's Control Over BCBSM Is An Unconstitutional "Taking"

The critical issue under the Taking Clause is whether the governmental action has gone beyond "regulation" so as to become a "taking." *Ruckelshaus* v. *Monsanto Co.*, 104 S. Ct. 2862, 2875 (1984). Michigan's attempt to wrest control of BCBSM from its corporate membership clearly transcends "regulation"; it differs from "regulation" not only in degree but in kind.

A look at PA 350 itself reveals the vast qualitative difference in this case between "regulation" and "taking." It was *regulation* when the legislature set standards and authorized the Commissioner of Insurance to regulate BCBSM's rates for health care services. It was *regulation* when the legislature established definite cost containment goals governing provider reimbursement and procedures—including possible Commissioner intervention—to assure that BCBSM would achieve those goals. It was arguably *regulation* even when the legislature mandated that subscriber and public representation be increased on BCBSM's board of directors. However, it constituted a *taking* when the legislature stripped the corporate

membership of its right to elect those directors and control BCBSM's operations, and gave that property right to others.

Lest it be thought that the degree of government regulation in this case renders private control unimportant, the fact of the matter is that BCBSM retains broad discretionary authority to run the business. The Michigan Supreme Court squarely held:

> "Under our interpretation of the act, BCBSM's managerial power over its lines of business, subscriber certificates, and provider reimbursement contracts has not been preempted by the Insurance Commissioner. BCBSM still has the power to establish its lines of business, § 205(4), to establish and set rates for subscriber certificates, § 607(1), to enter into provider class plans, § 502(1), and to formulate its methods of provider reimbursement in accordance with the 'access,' 'quality,' and 'cost' goals of the act, § 504(1)." 422 Mich. at 48.

The short of the matter is that under the new statutory scheme of things, BCBSM's corporate membership will be disenfranchised and will lose control over vitally important discretionary decisionmaking.

The court below missed the mark completely when it declared that "losses incident to the lawful exercise of the police power are noncompensable," 422 Mich. at 46. Plainly, a valid regulatory purpose does not immunize governmental action against a Taking Clause challenge.

The Taking Clause itself states that private property may not be taken "for public use, without just compensation." And since the scope of "public use" is "coterminous with the scope of a sovereign's police powers," every compensable taking presupposes a lawful exercise of the police power. *Hawaii Housing Authority* v. *Midkiff*, 104 S. Ct. 2321, 2329 (1984). *Accord, Ruckelshaus* v. *Monsanto Co.*, 104 S. Ct. 2862, 2879 (1984); *Berman* v. *Parker*, 348 U.S. 26, 33 (1954). As this Court recently explained, "[i]t is a *separate question* . . . whether an otherwise valid regulation so frustrates property

rights that compensation must be paid." *Loretto* v. *Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 425 (1982) (emphasis added). *Accord, Ruckelshaus* v. *Monsanto Co.*, 104 S. Ct. 2862, 2880 (1984).

The key question in this case, therefore, is not whether there has been a valid exercise of the police power, as the Michigan Supreme Court erroneously assumed, but whether the legislature, in its zeal to regulate, has overstepped the bounds of regulation and has taken property—albeit for public use—without just compensation.

To be sure, there is no "set formula" to apply in answering that question; the inquiry is essentially *ad hoc*. *Ruckelshaus* v. *Monsanto Co.*, 104 S. Ct. 2862, 2874 (1984); *Kaiser Aetna* v. *United States*, 444 U.S. 164, 175 (1979). But in making that inquiry, this Court has focused "both on the character of the [governmental] action and on the nature and extent of the interference" with the property interests involved. *Penn Central Transportation Co.* v. *New York City*, 438 U.S. 104, 130 (1978). Here, Michigan is depriving BCBSM's corporate membership of its *entire* property interest, not just one strand in its bundle of rights. All of its rights of governance are being taken away: its right to choose the board of directors, to amend the articles of incorporation and bylaws, and to determine its own composition and succession. Under PA 350, the corporate membership becomes a vestigial body with no authority whatsoever.

But PA 350 does not stop there. It creates a *new* corporate membership, to be selected in the same manner as the board of directors. The current membership is not permitted to have any role in selecting its successors. Thus, members of BCBSM are not only being stripped of all of the rights they now enjoy, but are losing their very membership.

This is not a case, therefore, where a private party retains some measure of dominion over the property which was allegedly taken. Rather, PA 350 "chops through the bundle" of property rights, extinguishing the fundamental rights of

BCBSM's corporate membership "to possess, use and dispose." *See Loretto* v. *Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 435 (1982). The corporate membership has been utterly deprived of its property; it has retained nothing.[11]

The court below nevertheless thought that there was no taking under *Penn Central* because, according to the majority, BCBSM's corporate membership had no "investment-backed expectations" in controlling the affairs of BCBSM.[12] However, nonprofit corporations, by definition, do not make "investments" in a profit-making sense. It cannot be the law that the property of a nonprofit corporation is therefore not entitled to any constitutional protection. Rather, governmental appropriation of property which is privately held for nonprofit purposes must be subject to the same standards that are applicable to all takings.

Unless the government is free to seize the assets of nonprofit corporations at will without payment of compensation, one may not give the phrase "investment-backed expectation" the wooden reading given by the court below. Neither a corporation nor its membership needs to have a *direct pecuniary interest in profits* to have an "investment-backed expectation."[13]

As Justice Levin pointed out, BCBSM's membership *did* make substantial investments in the corporation. The initial working capital of BCBSM's corporate predecessors was contributed by the founding hospitals and physicians. Those who made the investment had a right to expect that control of the

---

11 This critical fact distinguishes such cases as Andrus v. Allard, 444 U.S. 51 (1979), and Penn Central Transportation Co. v. New York City, 438 U.S. 104 (1978).

12 *Penn Central* identified several factors for determining whether a governmental action constitutes a "taking," including its interference with "investment-backed expectations." 438 U.S. at 124.

13 Indeed, "the interest in anticipated gains has traditionally been viewed as less compelling than other property-related interests." Andrus v. Allard, 444 U.S. 51, 66 (1979).

corporation would remain in the hands of their chosen successors.

Moreover, "investment" encompasses more than investment of money. As this Court has recently observed, property "includes the products of an individual's 'labour and invention.' " *Ruckelshaus* v. *Monsanto Co.*, 104 S. Ct. 2862, 2873 (1984), citing 2 W. Blackstone, Commentaries, *405 and J. Locke, The Second Treatise of Civil Government, ch. 5 (J. Gough ed. 1947). BCBSM's growth and success has been due in no small measure to years of labor, innovation and initiative contributed by BCBSM's members. Indeed, the court below recognized that BCBSM's success is partially attributable to "the expertise and aggressiveness of its management" (422 Mich. at 15)—management which was chosen by BCBSM's directors who, in turn, were elected by and accountable to the corporate membership.

It is quite evident, moreover, that BCBSM's members expected tangible benefits from their investment of time, money and effort in BCBSM's future. All constituent groups which comprise BCBSM's membership have an intense economic interest in BCBSM's destiny. The group subscribers, including employers and unions, engage in collective bargaining over the level and type of benefits provided, and those benefits are an important part of the overall package of rights and obligations ultimately negotiated between labor and management. Individual subscribers, of course, also have an economic interest in what they are going to pay for, and what they are going to receive in, health care service. Finally, providers have the same continuing economic interest which caused them to establish BCBSM in the first place: to avoid the financial uncertainty resulting from the inability of the needy to pay for health care. Thus, all of the constituent elements of BCBSM's corporate membership have vitally important economic interests in BCBSM—interests which motivated them to invest many years of service and hard work in the enterprise.

The assumption of the court below that the corporate membership had no reasonable expectation of continued con-

trol is simply incorrect. Although BCBSM has always been subject to some degree of government regulation, the regulatory framework left, and still leaves, wide room for management initiative. 422 Mich. at 48-49; *Blue Cross and Blue Shield of Michigan* v. *Demlow*, 403 Mich. 399, 429, 270 N.W.2d 845, 855 (1978). While BCBSM's membership could expect changes in regulatory requirements and constraints, nothing presaged Michigan's attempt to wrest control of BCBSM from its lawful owners. In a very real sense, therefore, PA 350 subverts the reasonable, investment-backed expectations of BCBSM's corporate membership.

In sum, the character of the governmental action—transferring control of a corporation—goes well beyond regulation; its impact on the property interests of BCBSM's membership is absolute; and it interferes with substantial investment-backed expectations. Accordingly, those sections of PA 350 which divest the corporate membership of its rights to elect the board of directors (§ 301(7)), to determine its own members (§ 305(1)), and to amend the articles of incorporation and corporate bylaws (§§ 203, 302(1)), constitute an unconstitutional taking of private property unless just compensation is paid.

3. Since Michigan Has Not Provided For Just Compensation, BCBSM Is Entitled To An Injunction

Michigan has not offered to compensate BCBSM's membership for the taking of its property. Moreover, it has no mechanism for post-taking compensation. 422 Mich. at 98 n.4. BCBSM is accordingly entitled to an injunction to prevent an uncompensated, unconstitutional taking of its private property.

CONCLUSION

For the reasons stated above, this Court should note probable jurisdiction of this appeal.

Dated: July 25, 1985

Respectfully submitted,

STANLEY D. ROBINSON
Kaye, Scholer, Fierman,
Hays & Handler
425 Park Avenue
New York, New York 10022
(212) 407-8000

Attorney for Appellant

Of Counsel:
Randolph S. Sherman
Joel Katcoff

Of Counsel:
William A. Saxton
Keefe A. Brooks
Butzel Long Gust Klein
& Van Zile
1881 First National Building
Detroit, Michigan 48226
(313) 963-8142